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No. 488

In the Supreme Court of the United States

OCTOBER TERM, 1942

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHICAGO STOCK YARDS COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

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The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the First Circuit entered in the above cause on July 24, 1942.

OPINIONS BELOW

The opinions in the United States Board of Tax Appeals (3 R. 932–956), are reported in 41 B. T. A. 590. The opinion of the Circuit Court of Appeals (4 R. 1265–1297) is not yet reported.

JURISDICTION

The judgment of the Circuit Court of Appeals for the First Circuit was entered July 24, 1942 (4 R. 1298). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Circuit Court of Appeals improperly rejected findings of the United States Board of Tax Appeals, (a) that during the taxable years in question the taxpayer was a mere holding or investment company, (b) that it permitted its gains and profits to accumulate beyond the reasonable needs of its business, and (c) that it was availed of for the purpose of preventing the imposition of the surtax upon its shareholders, within the meaning of Section 104 of the Revenue Acts of 1928 and 1932.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

> SEC. 104. ACCUMULATION OF SURPLUS TO EVADE SURTAXES.
>
> (a) If any corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there shall be levied, collected, and paid for each taxable year upon the net

income of such corporation a tax equal to 50 per centum of the amount thereof, which shall be in addition to the tax imposed by section 13 and shall be computed, collected, and paid upon the same basis and in the same manner and subject to the same provisions of law, including penalties, as that tax.

(b) The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to escape the surtax.

(c) As used in this section the term "net income" means the net income as defined in section 21, increased by the sum of the amount of the dividend deduction allowed under section 23 (p) and the amount of the interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner.

(d) The tax imposed by this section shall not apply if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire distributive shares, whether distributed or not, of the net income of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corpora-

> tion out of the earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

The provisions of Section 104 of the Revenue Act of 1932, c. 209, 47 Stat. 169, are identical with those of Section 104 of the Revenue Act of 1928, except as subdivision (a) of Section 104 of the Revenue Act of 1932 was amended by Section 214 of the National Industrial Recovery Act (c. 90, 48 Stat. 195) which provides as follows:

> SEC. 214. Section 104 of the Revenue Act of 1932 is amended by striking out the words "the surtax" wherever occurring in such section and inserting in lieu thereof "any internal-revenue tax." The heading of such section is amended by striking out "surtaxes" and inserting in lieu thereof "internal-revenue taxes." Section 13 (c) of such Act is amended by striking out "surtax" and inserting in lieu thereof "internal-revenue tax."

The Treasury regulations applicable to Section 104 are set forth in the Appendix, *infra*, pp. 24–27.

STATEMENT

The central question involved is whether the taxpayer corporation, Chicago Stock Yards Company, was "availed of" during the years 1930, 1932, and 1933 for the purpose of preventing the imposition of surtax upon its stockholders by per-

mitting its gains and profits to accumulate instead of being distributed. The Commissioner determined that the corporation had been availed of for that purpose, and accordingly proposed to assess the 50% tax imposed by Section 104 of the Revenue Acts of 1928 and 1932. (3 R. 932–933.) The Board of Tax Appeals affirmed the Commissioner's determination, and approved the imposition of additional taxes for the years involved, aggregating in excess of $4,000,000 plus interest (3 R. 958, 1238–1239, 1240). It made extensive findings of fact (3 R. 902–932), which may be summarized as follows:[1]

The Chicago Stock Yards Company is a Maine corporation; it was organized in 1911 (3 R. 902), at which time Mr. Frederick H. Prince became the owner of 80.6% of its capital stock.[2] He acquired the remaining stock in 1922 (3 R. 909) with funds advanced to him by the corporation (3 R. 926), and throughout the years in question continued to own or control 100% of the stock.[3]

[1] In view of the complexity of the findings, it is not feasible to recount all the details. The summary set forth above is intended as an outline of the important relevant facts, but since respondent may disagree as to what are the important relevant facts, we respectfully refer the Court to the findings themselves (3 R. 902–932) for a complete statement.

[2] Of the 80,000 shares issued, Prince became the owner of 64,480 shares in November, 1911 (3 R. 907–908). In June 1922, he became the owner of the remaining 15,520 shares (3 R. 909).

[3] In 1932, he transferred a substantial portion of the stock to F. H. Prince & Co., Inc., a corporation owned entirely by himself, and then transferred the F. H. Prince & Co., Inc. stock to himself and his wife as trustees for the benefit of

The taxpayer is the top holding company of what is referred to as the Chicago Stock Yards enterprise, a great integrated business owning or operating a stockyard, a belt line railway, an elevated street railway, a real estate development of considerable magnitude, power and light facilities, a national bank serving the stockyard area, and other related undertakings of lesser importance. For the convenience of the Court, we have annexed a diagram, adopted by the court below, showing the organization of the entire enterprise as of December 31, 1933. Although several of the undertakings are under the control of corporations immediately owned by the taxpayer (for example, the power and light activities are conducted by the Produce Terminal Corporation, which is wholly owned by the taxpayer), the great bulk of the enterprise is concentrated in corporations and a Massachusetts trust that are wholly owned by an intermediate holding company, the Chicago Junction Railways and Union Stock Yards Company, a New Jersey corporation, referred to as the Jersey Company.[4]

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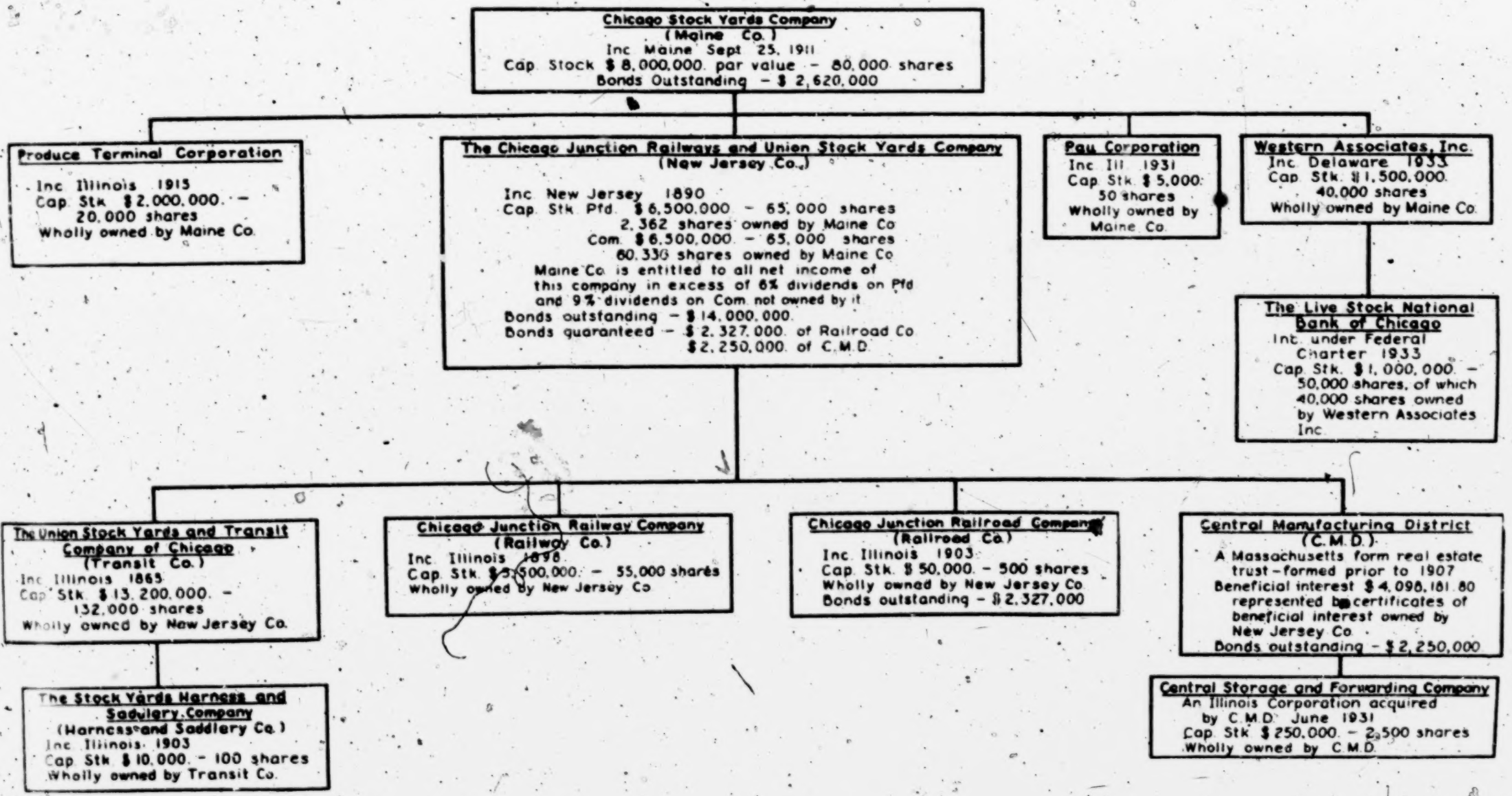
certain relatives and friends (3 R. 910). Mr. Prince thus retained the power to vote the stock, and as a result remained in complete control of the taxpayer. As pointed out by the court below (4 R. 1269), the 1932 change of stock ownership "is assumed by both parties to be immaterial to the present litigation."

[4] The Jersey Company was organized in 1890 with a corporate life of 50 years (3 R. 902). Its principal subsidiaries are as follows:

(1) The Union Stock Yards and Transit Company of Chicago, referred to as the *Transit Company*, operated the

CHICAGO STOCK YARDS ENTERPRISE

December 31, 1933


Chicago Stock Yards Company
(Maine Co.)
Inc Maine Sept 25, 1911
Cap Stock $8,000,000 par value – 80,000 shares
Bonds Outstanding – $2,620,000
Produce Terminal Corporation
Inc Illinois 1915
Cap Stk $2,000,000. – 20,000 shares
Wholly owned by Maine Co.
The Chicago Junction Railways and Union Stock Yards Company
(New Jersey Co.)
Inc New Jersey 1890
Cap Stk Pfd $6,500,000 – 65,000 shares
2,362 shares owned by Maine Co
Com $6,500,000 – 65,000 shares
60,330 shares owned by Maine Co
Maine Co is entitled to all net income of this company in excess of 6% dividends on Pfd and 9% dividends on Com not owned by it
Bonds outstanding – $14,000,000.
Bonds guaranteed – $2,327,000 of Railroad Co
$2,250,000 of C.M.D.
Pau Corporation
Inc Ill 1931
Cap Stk $5,000
50 shares
Wholly owned by Maine Co.
Western Associates, Inc.
Inc Delaware 1933
Cap Stk $1,500,000
40,000 shares
Wholly owned by Maine Co.
The Live Stock National Bank of Chicago
Int. under Federal Charter 1933
Cap Stk $1,000,000 – 50,000 shares, of which 40,000 shares owned by Western Associates Inc.
The Union Stock Yards and Transit Company of Chicago
(Transit Co.)
Inc Illinois 1865
Cap Stk $13,200,000 – 132,000 shares
Wholly owned by New Jersey Co.
Chicago Junction Railway Company
(Railway Co.)
Inc Illinois 1898
Cap Stk $5,500,000 – 55,000 shares
Wholly owned by New Jersey Co
Chicago Junction Railroad Company
(Railroad Co.)
Inc Illinois 1903
Cap Stk $50,000 – 500 shares
Wholly owned by New Jersey Co
Bonds outstanding – $2,327,000
Central Manufacturing District
(C.M.D.)
A Massachusetts form real estate trust – formed prior to 1907
Beneficial interest $4,098,181.80 represented by certificates of beneficial interest owned by New Jersey Co.
Bonds outstanding – $2,250,000
The Stock Yards Harness and Saddlery Company
(Harness and Saddlery Co.)
Inc Illinois 1903
Cap Stk $10,000. – 100 shares
Wholly owned by Transit Co.
Central Storage and Forwarding Company
An Illinois Corporation acquired by C.M.D. June 1931
Cap Stk $250,000 – 2,500 shares
Wholly owned by C.M.D.

The capital stock of the Jersey Company consisted of 65,000 shares of common and 65,000 shares of voting preferred. In addition it had a bonded indebtedness of $14,000,000 which was to mature in 1940. (3 R. 903.) By December 31, 1929, the taxpayer had acquired 58,472 shares of the Jersey

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stockyards. It was organized as an Illinois corporation in 1865. During the years 1911–1913 more than 98 percent of its capital stock was owned by the Jersey Company, and since that time it has been wholly owned by the Jersey Company. It had debenture notes outstanding in the amount of $500,000, which were paid off in 1930, and it has had no bond or note obligations thereafter. (3 R. 902.)

(2) The Chicago Junction Railway Company, referred to as the *Railway Company*, owned a railroad which served the stockyards. It was organized as an Illinois corporation in 1898, and is wholly owned by the Jersey Company. It leased its railroad to the Transit Company at an annual rental of $600,000, which in turn leased it to a subsidiary of the New York Central Railroad at an annual rental of $2,000,000. During the years 1930–1933, it had no outstanding indebtedness. (3 R. 903–904.)

(3) The Chicago Junction Railroad Company, referred to as the *Elevated Company* or the Railroad Company, owned and operated an elevated railroad serving Packingtown, an area where the large meat packing companies had their plants, located in Chicago west of the stockyards. It was organized in 1902 and has always been wholly owned by the Jersey Company. It had outstanding bonds in the principal amount of $2,327,000, due in 1945. These bonds were guaranteed by the Jersey Company. (3 R. 904–905.)

(4) The Central Manufacturing District, referred to as the *District*, a Massachusetts trust wholly owned by the Jersey Company, owned extensive real estate adjacent to the stockyards. It had its own streets and police, water, lighting, and sewerage facilities. It had bonds outstanding which ranged from $2,915,000 in principal amount in 1930, to $2,250,000 in principal amount in 1933. These bonds were guaranteed by the Jersey Company. (3 R. 905.)

Company's common and 457 shares of the preferred (3 R. 912). During the period here in controversy, 1930–1933, the taxpayer added to its holdings in the Jersey Company, and at the end of 1933, it held 60,336 shares of common and 2,362 shares of preferred (3 R. 927–928).[5]

On October 1, 1914, the taxpayer and the Jersey Company had entered into an agreement (referred to as the bypass agreement), whereby the taxpayer guaranteed the interest, but not the principal, upon the $14,000,000 bonds of the Jersey Company and upon the $2,327,000 bonds of the Elevated Company; it also guaranteed a $6 dividend upon the Jersey Company's preferred stock and a $9 dividend upon its common.[6] On its part, the Jersey Company assigned to the taxpayer its right to all dividends received from its subsidiaries, and directed the Railway Company to apply the $600,000 received as annual rental for its railroad, to interest on the Jersey Company's bonds. The Jersey Company further agreed to use its income

[5] Thus, it purchased 253 shares of common in 1930, 604 shares in 1931, 380 shares in 1932, and 357 shares in 1933; and it purchased 190 shares of preferred in 1930, 616 shares in 1931, 302 shares in 1932, and 797 shares in 1933 (3 R. 927–928).

[6] Upon formation of the taxpayer in 1911, the common stock holders of the Jersey Company were given the option of exchanging their stock for bonds of the taxpayer or retaining the stock and accepting the taxpayer's guaranty of a $9 annual dividend but assigning any excess to the taxpayer (3 R. 906–907).

first to pay its own expenses and taxes, and then to pay the surplus to the taxpayer upon its request. (3 R. 908.) The taxpayer has never been called upon to make any payments pursuant to its guarantees (3 R. 931).

On December 31, 1929, the Jersey Company and its subsidiaries had total net consolidated assets in the amount of $73,322,871.58 and net consolidated liabilities in the amount of $33,194,175.08, leaving an excess of over $40,000,000 in assets (3 R. 913). In addition, Produce Terminal Corporation, owned directly by the taxpayer, was a prosperous corporation, with over $2,500,000 in assets in excess of liabilities (3 R. 912–913). On December 31, 1929, the taxpayer itself had an earned surplus and an excess of assets over all liabilities (including its capital stock) of over $19,000,000 (3 R. 912–913). Its bonded indebtedness at that time was $3,227,000 (3 R. 913), and it had liquid assets of nearly $12,000,000[7] (3 R. 914).

The total net earnings of the taxpayer for the four years, 1930–1933, were $10,243,373.01, and out of these earnings it paid an aggregate of only $1,600,000 in dividends (3 R. 919). The net income of the taxpayer and the dividends paid by it during

[7] Produce Terminal Corporation together with the Jersey Company and its subsidiaries had additional liquid assets in the amount of about $10,000,000. This latter figure, however, includes certain impounded charges in the amount of about $2,000,000 which were not released to the Transit Company until 1932 (3 R. 914).

the years 1911–1933 are shown by the following tabulation (3 R. 918):

Year	Net earnings	Dividends paid	Excess of net earnings
1911–1929	$24,373,905.69	$4,790,000	$19,615,905.69
1930	3,468,336.80	400,000	3,068,336.80
1931	2,378,232.14	400,000	1,978,232.14
1932	2,172,963.09	400,000	1,772,963.09
1933	2,243,840.98	400,000	1,843,840.98
	34,637,278.70	6,390,000	28,259,278.70

During the years 1930–1933, inclusive, and prior thereto, the principal activity of the taxpayer was the purchase and holding of securities and the collecting of dividends thereon, together with the lending of money to Mr. Prince (3 R. 931). In its income tax returns for those years it described its business as that of "acquiring and guaranteeing securities" (3 R. 931–932).

The taxpayer's income during the years 1930–1933 consisted exclusively of interest, dividends, and profit upon sale of securities. It received no fees for the management and supervision of any of its subsidiaries. It had practically no office expenses; it paid no rent except vault rent, and its office was Prince's office at 1 Court Street, Boston. It paid its treasurer a salary of $500 per annum and "wages" of $2,000 per annum. Apart from the $50,000 salary which it paid to its president, Prince, it paid no other salaries or wages. McDonough, its vice president and Prince's secretary, did not receive any salary from the taxpayer. (3 R. 937.)

Moreover, in addition to his salary from the taxpayer, Prince received the following annual salaries from the taxpayer's affiliates in the capacities indicated below (3 R. 929):

President of the Jersey Co.	$17,500.00
Chairman of the board of directors of the Transit Co.	17,500.08
Chairman of the board of directors of the Railway Co.	12,499.92

And although Prince actively supervised the operations of the Jersey Company and its subsidiaries as well as the subsidiaries of the taxpayer, he was enabled to do so through his ownership of all the taxpayer's stock. Furthermore, in the light of the salaries received by Prince from the Jersey Company, the Railway Company, and the Transit Company, the Board found that when he was directing the affairs of those companies, he was acting as a paid employee of those companies and not of the taxpayer. (3 R. 938.)*

The taxpayer made many cash loans to Prince over the period of its existence, and Prince's in-

* Some of the facts stated in the above paragraph are not separately denominated as "findings" by the Board, but appear in the body of its opinion at 3 R. 937, 938. However, it is settled that determinations of fact, even though in the body of the Board's opinion, must be treated as findings. *Sheppard & Myers, Inc.* v. *Commissioner*, 45 F. (2d) 50 (C. C. A. 3d), certiorari denied, 282 U. S. 902; *Emerald Oil Co.* v. *Commissioner*, 72 F. (2d) 681 (C. C. A. 10th); *American Textile Woolen Co.* v. *Commissioner*, 68 F. (2d) 820 (C. C. A. 6th), certiorari denied, 293 U. S. 558; *Olson* v. *Commissioner*, 67 F. (2d) 726 (C. C. A. 7th), certiorari denied, 292 U. S. 637; *Insurance & Title Guarantee Co.* v. *Commissioner*, 36 F. (2d) 842 (C. C. A. 2d), certiorari denied, 281 U. S. 748.

debtedness to the taxpayer rose from $2,529,400 in 1930 to $4,848,000 in 1933 (3 R. 916). The loans were used by Prince for any purpose he desired.[9] Thus, Prince borrowed $160,000 from the taxpayer in 1932 for the purchase of a home in Newport, Rhode Island, and $450,000 in order to strengthen the financial statement of F. H. Prince & Co. which he was required to file with the New York Stock Exchange.[10] In 1933 he borrowed an additional $440,000 for the same purpose, and $1,000,000 to purchase stock in Armour & Co.[10] (3 R. 917.)

The taxpayer's failure to distribute its earnings during the years in question resulted in Prince's avoidance of large surtaxes during each of the years (3 R. 930–931).

In addition to its numerous subsidiary findings, the Board made three critical ultimate findings (3 R. 932):

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[9] Prince's relationship to the taxpayer is further illuminated by the fact that during the years 1930–1933 he transferred various securities to it, apparently unrelated to the stockyards enterprise, and thereby established losses which he deducted from his taxable income for those years (3 R. 928–929).

[10] The acquisition of the Armour stock enabled him to become chairman of its board of directors (3 R. 917). The practice had grown up during the years 1930–1932 among the packers whereby livestock would be shipped directly from the farmers to smaller stockyards and would then be conveyed by truck to the packing houses, thus avoiding the Chicago stockyards entirely. Prince's position as chairman of the board of directors of Armour made it possible for him to retain Armour's business for the Chicago stockyards. (3 R. 926.)

44. During the years 1930, 1932, and 1933 the petitioner was a mere holding or investment company.

45. During the years 1930, 1932, and 1933 the petitioner permitted its gains and profits to accumulate beyond the reasonable needs of its business.

46. During the years 1930, 1932, and 1933 the petitioner was availed of for the purpose of preventing the imposition of the surtax upon its stockholders through the medium of permitting its gains or profits to accumulate instead of being divided or distributed.

These three separate findings formed the basis for its decision against the taxpayer on three independent grounds: (1) that since the taxpayer was a "mere holding company," the presumption set forth in Section 104 (b) was operative and that the evidence failed to rebut that presumption (3 R. 939); (2) that the accumulation of profits beyond the taxpayer's reasonable needs similarly brought the same presumption into play, and that the evidence, carefully reviewed on this aspect of the case (3 R. 940–945),[11] likewise failed to rebut

[11] On this aspect of the case, the Board determined that the taxpayer had no need for such accumulation of profits as a holding company (3 R. 940–941), and that it had no need for them as a management company or for the purpose of financing its affiliates (3 R. 941). And the Board finally determined that Prince's desire to buy out the various other stockholders in the Jersey Company by 1940, when its charter would expire, and to pay off all the bonded indebtedness of the entire Chicago Stockyards enterprise so that he might become its sole owner by 1940, was not, in the circumstances of this case, within the reasonable needs of the taxpayer's business (3 R. 942–945).

the presumption; and (3), that in any event, even without the benefit of the statutory presumptions, the record fully supports the ultimate determination that the taxpayer was "availed of" within the meaning of Section 104 (a) for the condemned purpose (3 R. 945–950).

The Circuit Court of Appeals reversed. It first rejected the Board's determination that the taxpayer was a "mere holding company," and treated the taxpayer as though it were, through Prince, an active corporation in the stockyards enterprise. The court thus ignored the Board's specific determinations that Prince's participation in the affairs of the Jersey Company, the Transit Company, and the Railway Company was as a paid employee of those companies and not as an officer of the taxpayer. Secondly, the court rejected the Board's second ultimate finding that the taxpayer's profits were permitted to accumulate beyond the reasonable needs of its business. In so doing, the court itself determined that the "liquidation" of the Jersey Company by 1940 was within the reasonable needs of the taxpayer's business, and it simply remanded the case to the Board for further findings as to the amount of profits that it was necessary to retain, for the projected "liquidation" of the Jersey Company and for the eventual extinguishment of all debts of the enterprise. Thirdly, the court rejected the Board's final finding that irrespective of the taxpayer's status as a "mere holding company" and irrespective of the character of the

accumulation, the corporation was in fact "availed of" in order to prevent the imposition of surtax upon its stockholders.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In overturning the determination of the Board of Tax Appeals that the respondent was a mere holding or investment company.

2. In overturning the Board's determination that respondent had accumulated its gains and profits beyond the reasonable needs of its business.

3. In overturning the Board's determination that respondent was availed of for the purpose of preventing the imposition of the surtax upon its stockholders through the medium of permitting its gains or profits to accumulate instead of being divided or distributed.

4. In failing to accord the full effect to the presumption established by Section 104 (b).

5. In holding that the projected 1940 liquidation of the Jersey Company, coupled with the acquisition of sufficient Jersey common and preferred stock to be able to control the liquidation, was a reasonable need of the respondent's business.

6. In remanding the case upon a false issue.

7. In reversing the judgment of the Board.

REASONS FOR GRANTING THE WRIT

In reversing the decision of the Board, the court below improperly rejected three critical findings of fact, any one of which, standing alone, was suffi-

cient to support the Board's decision. We think that the action of the court below was such as to call for review by this Court. Cf. *Helvering* v. *National Grocery Co.*, 304 U. S. 282.

1. After making certain important subsidiary findings (3 R. 931), the Board specifically found that the taxpayer was a "mere holding company" (3 R. 932). Moreover, in its opinion, it indicated some of the considerations which led it to make that finding, and in particular it stated (3 R. 937, 938):

> The petitioner's income during the years 1930 to 1933 consisted exclusively of interest, dividends, and profits from the sale of securities. It received no fees for the management and supervision of other corporations. Its office was Prince's office at 1 Court Street, Boston, Massachusetts. An inspection of its income tax returns shows that it had practically no office expenses. It paid no rent except vault rent. It paid its president a salary of $50,000 per annum, its treasurer a salary of $500 per annum, and "wages" of $2,000 per annum. It paid no other salaries or wages. McDonough was Prince's secretary and was also vice president of the petitioner. He did not, however, receive any salary from the petitioner.
>
> * * * * *
>
> It is true, of course, that Prince supervised the operations of the Jersey Co. and all of its subsidiaries as well as of the subsidiaries of the petitioner. He was enabled to do this through ownership of all the stock of the petitioner, which had virtual control

through stock ownership of the other corporations. He was president of the Jersey Co., from which he received an annual salary of $17,500. He was also chairman of the board of directors of the Transit Co., from which he received a like salary, and chairman of the board of directors of the Railway Co., from which he received a salary of $12,499.92. He dictated the policies of the petitioner and of all of the other companies. It does not appear, however, that the petitioner supervised and managed the operations of its subsidiaries and those of the Jersey Co. and its subsidiaries. Prince did this himself. So far as appears, there were no meetings of the board of directors of the petitioner for the determination of any acts to be done by any of the companies. The returns of the Transit Co. and the Railway Co. report Prince as devoting 58 percent of his time to the affairs of the former and 42 percent to the latter. *When directing the affairs of those companies Prince was acting as a paid employee of those companies and not of the petitioner.* [Italics supplied.]

The court below, however, rejected the finding of the Board that the taxpayer was a "mere holding company." It stated: "We do not think that this is a permissible finding on the record, particularly in view of the subsidiary facts found by the Board" (4 R. 1285). The court then went on to find that, in its view of the record, the taxpayer was actively involved in the operation of the stockyards enter-

prise. It concluded that Prince's activities in the enterprise were to be attributed to the taxpayer, and in so doing it stressed one of the subsidiary findings of the Board that "representatives" of the taxpayer went to Chicago, giving orders and directions. However, it is perfectly plain from the Board's findings and its opinion, that it was referring to Prince (and possibly also to his assistant, McDonough), and that it regarded Prince's participation in the enterprise as being outside his capacity as an officer of the taxpayer. In finding otherwise, the court weighed the evidence and drew inferences from the facts. This it was not at liberty to do. *Wilmington Trust Co.* v. *Commissioner*, 316 U. S. 164; *Helvering* v. *National Grocery Co.*, *supra*. The finding of the Board in this case that the taxpayer was a "mere holding company" was just as much a finding of fact as its determination in the *Wilmington Trust Co.* case that a certain transaction was a "short sale". If the reviewing court had no authority to reject the finding in that case, there was similarly no authority to do so here. Cf. also *Elmhurst Cemetery Co.* v. *Commissioner*, 300 U. S. 37; *Helvering* v. *Lazarus & Co.*, 308 U. S. 252; *Helvering* v. *Kehoe*, 309 U. S. 277; *Colorado Bank* v. *Commissioner*, 305 U. S. 23. Moreover, on this phase of the case, the court did not appear to leave any room for further consideration by the Board upon remand as to whether the taxpayer was a "mere holding company", as it should have done if it were otherwise

correct in concluding that the Board's finding was not properly supported. *Helvering* v. *Rankin*, 295 U. S. 123, 131. The court itself had no power to make the ultimate determination. *Helvering* v. *National Grocery Co.*, 304 U. S. at 294–295.

2. An additional reason for review in connection with the court's rejection of the first critical finding, is its treatment of the presumption which that finding called into play. Section 104 (b) provides that "The fact that any corporation is a mere holding or investment company * * * shall be prima facie evidence of a purpose to escape the surtax." The court held that since the taxpayer has the burden of proving the Commissioner's determination erroneous in every tax case, the presumption established by Section 104 (b) "would seem not to amount to much." (4 R. 1285.) However, it is apparent that Congress was deeply concerned with avoidance of surtaxes through such corporations, and that it intended to cast a greater burden upon taxpayers in this type of case than is represented by the ordinary burden of going forward with the evidence. Otherwise, it would have been unnecessary to enact Section 104 (b). The issue is one of considerable importance because, if the decision is permitted to stand, it may erroneously influence the Board in its disposition of like cases, and its findings would obviously be such that the issue probably could never be

sharply raised in any of those cases by the Government in this Court. Accordingly, it is important that the question be considered now.

3. The Board's second critical finding rejected by the court below was that during the years in question the taxpayer "permitted its gains and profits to accumulate beyond the reasonable needs of its business." (3 R. 932.) The Board determined (3 R. 940-941) that the taxpayer had used its excess income to make additional investments and that this practice could not be regarded as within the reasonable needs of the business of a holding company. Even considered as a management company the Board concluded that the taxpayer had no need for the accumulation of so large a surplus (3 R. 941); that there was no need to accumulate profits for the purpose of financing other corporations (3 R. 941); that the taxpayer had used a large part of its profits in the purchase of the shares of stock in the Jersey Company (3 R. 942); that the next most important item consisted of loans made primarily to Prince (3 R. 942); that accumulations for the purpose of liquidating the Jersey Company in 1940 upon the expiration of its charter (including the acquisition of outstanding Jersey stock before that time and the accumulation of funds to pay off all bonds of Jersey and the taxpayer) were not within the reasonable needs of the business (3

R. 942–943); and that in view of the accumulations previously made there was no reasonable need for further accumulations during the taxable years (3 R. 943). Moreover, the Board expressly found that at the end of 1929 the taxpayer and its subsidiaries had over $19,000,000 available in liquid assets plus over $40,000,000 in fixed and other assets (3 R. 913–914), or a total of more than $60,000,000 in assets as against about $23,000,000 in bonded indebtedness (3 R. 913). By the end of 1933 the taxpayer's surplus had increased to over $28,000,000 (3 R. 919).

The court below reversed the ultimate finding of the Board. Its point of departure was that in its view, the "liquidation" of the Jersey Company by 1940 was within the reasonable needs of the taxpayer's business. Here again, its disagreement with the Board was upon a question of fact that the Board had determined after a most painstaking examination of the record. The remand to the Board upon this phase of the case leaves it to the Board to determine merely whether the accumulation was necessary for the liquidation of the Jersey Company and the eventual extinguishment of all the indebtedness of the enterprise, a false issue, for the Board had already found that the liquidation of the Jersey Company was not within the reasonable needs of the taxpayer's business.

4. Finally, the court below rejected the third critical finding of the Board that during the years involved (3 R. 932), the taxpayer "was availed of for the purpose of preventing the imposition of the surtax upon its stockholders through the medium of permitting its gains or profits to accumulate instead of being divided or distributed." The Board had indicated that this ultimate finding could rest either upon the statutory presumption called into play by the first two critical findings, or upon the record itself without the benefit of the presumptions. The Board unambiguously stated (3 R. 945):

> Even without the benefit of the statutory presumptions, we think there is sufficient evidence in the record to show the existence of the condemned purpose. The bare recital of the undisputed facts relating to the organization of the petitioner, the balance sheets, the source of earnings, the nature of the investments, the large accumulations of cash and surplus, the loans of cash and securities to the petitioner's sole stockholder, and the continued reinvestment of its gains and profits in securities, present, in our opinion, a situation typical of situations which Congress intended to cover by section 104 of the Revenue Acts of 1928 and 1932.

In rejecting this third finding, the court below simply substituted its judgment for that of the Board. The question is not whether the elements discussed by the court below would have justified

the Board in making a different finding; the essential consideration is that the Board did examine all the material before it and concluded as a matter of fact that the taxpayer had been "availed of" for the interdicted purpose. It was serious error to remand the case to the Board. *Helvering* v. *National Grocery Co.*, 304 U. S. at 295.

CONCLUSION

For the foregoing reasons, it is urged that this petition for certiorari be granted.

Respectfully submitted,

CHARLES FAHY,
Solicitor General.

OCTOBER 1942.

APPENDIX

Treasury Regulations 74 (promulgated under the Revenue Act of 1928):

ART. 541. TAXATION OF CORPORATION UTILIZED FOR EVASION OF SURTAX.—Section 104 is designed to discourage the formation or use of a corporation for the purpose of preventing the imposition of surtaxes upon its shareholders, through the device of permitting its gains and profits to accumulate instead of being distributed. If a domestic or foreign corporation is so formed or availed of, it is subject to a tax at the rate of 50 percent upon its net income in addition to the tax imposed by section 13. However, the additional tax at the rate of 50 percent does not apply for 1928 or any subsequent taxable year if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire distributive share, whether distributed or not, of the net income of the corporation for such year or years. Any amount so included in the gross income of a shareholder shall be treated as a dividend received, and any subsequent distribution made by the corporation out of the earnings or profits for such taxable years shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

ART. 542. PURPOSE TO ESCAPE SURTAX.—Prima facie evidence of a purpose to escape the surtax exists where a corporation is a

mere investment company, where a corporation has practically no business except holding stocks, securities, or other property and collecting the income therefrom or investing therein, or where a corporation other than a mere holding or investment company permits its gains and profits to accumulate beyond the reasonable needs of the business. The statutory presumption that a mere holding or investment company is subject to the additional tax imposed by section 104 may be overcome if the corporation can show, either by reason of the fact that it distributed a large portion of its earnings for the year in question, or that its stock was held not by the members of a family or of a small group but by a large number of persons and in comparatively small blocks, or by other evidence, that it was not availed of for the purpose of preventing the imposition of the surtax upon its shareholders.

The business of a corporation is not merely that which it has previously carried on, but includes in general any line of business which it may legitimately undertake. However, a radical change of business when a considerable surplus has been accumulated may afford evidence of a purpose to escape the surtax. When one corporation owns the stock of another corporation in the same or a related line of business and in effect operates the other corporation, the business of the latter may be considered in substance the business of the first corporation. Gains and profits of the first corporation put into the second through the purchase of stock or otherwise may therefore, if a subsidiary relationship is established, constitute employment of the income in its own business. To establish that the business of one corpo-

ration can be regarded as including the business of another it is ordinarily essential that the first corporation own substantially all of the stock of the second. Investment by a corporation of its income in stock and securities of another corporation is not without anything further to be regarded as employment of the income in its business.

ART. 543. UNREASONABLE ACCUMULATION OF PROFITS.—An accumulation of gains and profits is unreasonable if it is not required for the purposes of the business, considering all the circumstances of the case. It is not intended, however, to prevent reasonable accumulations of surplus for the needs of the business. No attempt can be made to enumerate all the ways in which gains and profits of a corporation may be accumulated for the reasonable needs of the business. Distributions made by a corporation shortly after the close of its taxable year shall be taken into consideration in determining the reasonableness of the amount of earnings and profits of the corporation retained by it for such year. Undistributed income is properly accumulated if invested in increased inventories or additions to plant reasonably needed by the business. It is properly accumulated if retained for working capital required by the business or in accordance with contract obligations placed to the credit of a sinking fund for the purpose of retiring bonds issued by the corporation. In the case of a banking institution the business of which is to receive and loan money, using capital, surplus, and deposits for that purpose, undistributed income actually represented by loans or reasonably retained for future loans is not accumulated beyond the reasonable needs of the business.

The nature of the investment of gains and profits is immaterial if they are not in fact needed in the business. It is an unreasonable accumulation of gains and profits by corporations with the purpose of enabling their shareholders to escape surtaxes on such gains and profits which subjects such corporations to the additional tax imposed by section 104. Among other things, the financial condition of the corporation at the close of the taxable year and the manner in which its funds are invested at that date, determine the reasonableness of the accumulations.

For the purpose of section 104 the term "net income" means the net income of the corporation as defined in section 21 increased by the sum of (1) the amount received as dividends and allowed as a deduction by section 23 (p), plus (2) the amount of interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner. The Commissioner, or any collector upon direction from the Commissioner, may require any corporation to furnish a statement of its accumulated gains and profits, the name and address of, and number of shares held by, each of its shareholders, and the amounts that would be payable to each, if the income of the corporation were distributed. (See section 149 (c).)

The like numbered Articles of Treasury Regulations 77 (promulgated under the Revenue Act of 1932) are substantially identical with the foregoing.

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